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WORKING CAPITAL

WORKING CAPITAL – DAY - 1

- DEFINITION OF WORKING CAPITAL
- FACTORS DETERMINING WORKING CAPITAL
- WORKING CAPITAL CYCLE / CASH CONVERSION CYCLE
- SOURCE OF WORKING CAPITAL FINANCEING
- WORKING CAPITAL PRODUCTS
- ASSESSMENT OF WORKING CAPITAL
- CREDIT MONITORING ARRANGEMENT
- FINANCIAL RATIOS

WORKING CAPITAL – DAY - 2

- SPECIAL SITUATIONS FOR ASSESSMENT OF WORKING CAPITAL
- MAXIMUM PERMISSIBLE BANK FINANCE (MPBF) - LIMITATION
- DRAWING POWER NOT ALLIGEND TO MPBF
- SECURITY
- WORKING CAPITAL VS. TERM LOAN
- LOAN DOCUMENTS PROCEDURE
- PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

LEARNING
AT THE END OF DAY - 1

- Basis of Working Capital
- Different component of the Working Capital / Working Capital Cycle
- Computation of the Working Capital
- Understanding of Various Ratios

LEARNING
AT THE END OF DAY - 2

- Practical problems in computation of Working Capital.
- Justification of shortfall in Drawing Power in various situations
- Brief of Securities
- Basic understanding of Loan Documents
- Outline of Detailed Project Report

DEFINITION OF WORKING CAPITAL

- Funds deployed for managing Business Operations.

- A Short Term Capital which provides MONEY to buy EARNING ASSETS.

- Working Capital refers to that part of the Capital, which is required for financing short-term or current assets such as Cash, Debtors and Inventories, Day to Day Operation etc.

- Funds thus invested in Current Assets keep REVOLVING FAST and are constantly converted into cash and this cash flows out again in exchange for other Current Assets.

DEFINATION OF WORKING CAPITAL

❖Working Capital refers to the cash a business requires for day-to-day operations, or, more specifically, for financing the conversion of raw materials into finished goods, which the company sells for payment. Among the most important items of working capital are levels of inventory, accounts receivable, and accounts payable.

❖Working Capital is also known as revolving or circulating capital or short-term capital.

❖It is the business's life blood.

FACTORS DETERMINING WORKING CAPITAL

- Types of Products Manufactured / Services rendered.
- Total Costs incurred on materials.
- Wages and overheads.
- The period of Raw materials holding before they are issued to production.
- The period of the Production Cycle or Work-in-progress / Stock-in-process, i.e., the time taken for conversion of raw materials to finished goods.
- The period of Finished goods holding i.e. finished goods are to be kept waiting for sales.
- The period of Receivable holding i.e. average period of credit allowed to customers.
- The amount of cash required to pay day-to-day expenses of the business / operation.
- The amount of cash required for advance payments, if any.
- The period of credit availed from suppliers.
- Time -lag in the payment of wages and other overheads.

WORKING CAPITAL CYCLE / CASH CONVERSION CYCLE (CCC)

It is the business's life blood. If a business is operating profitably, then it should, in theory, generate cash surpluses. If it doesn't generate surpluses, the business will eventually run out of cash and expire.

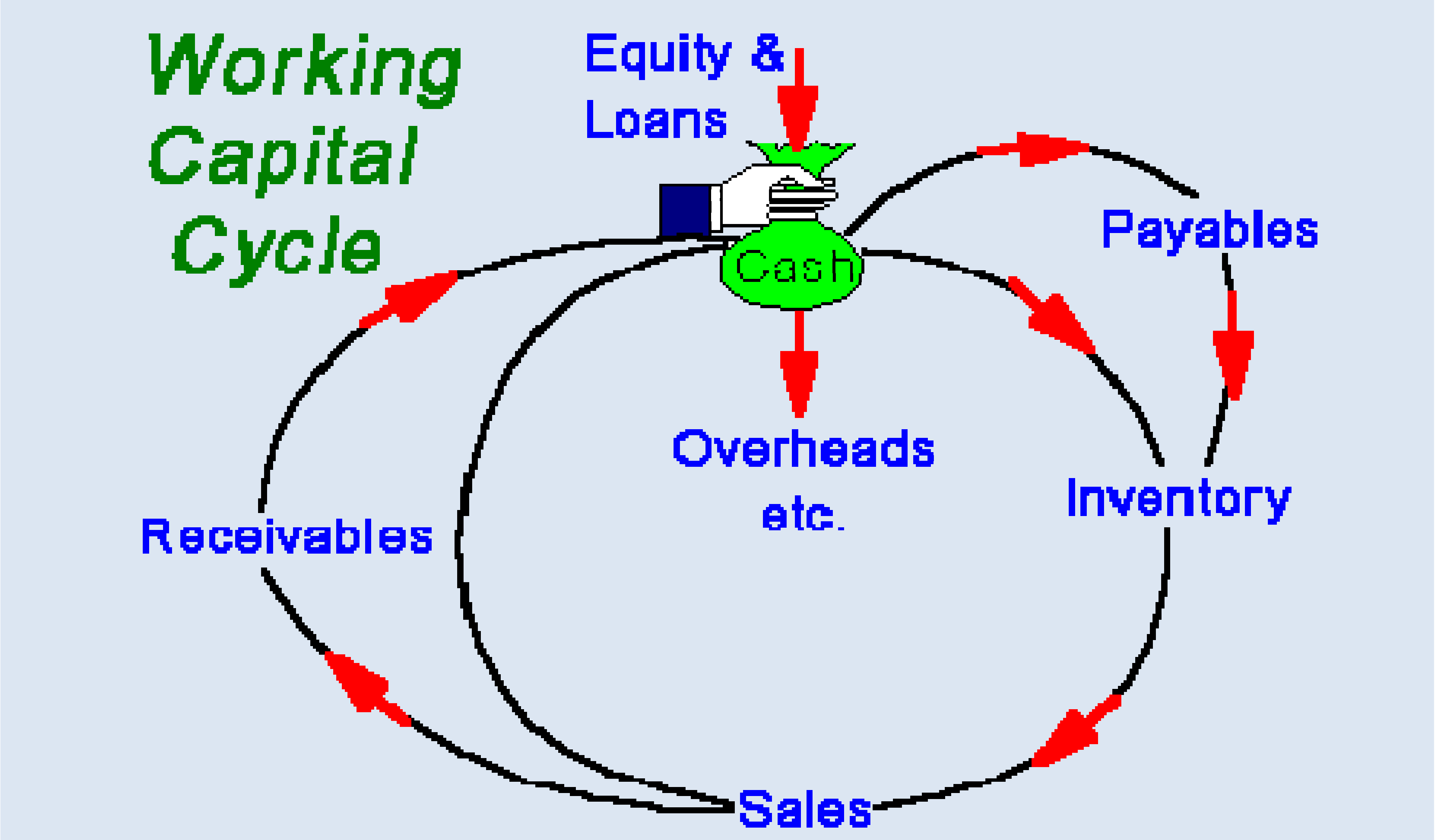
There are two elements in the business cycle that absorb cash -

- ❖**Inventory** (Raw Material, Work-in-progress, Finished Goods)
- ❖**Receivables** (Debtors owing you money).

The main sources of cash are –

- ❖**Payables** (your Creditors)
- ❖**Equity and Loans**.

WORKING CAPITAL CYCLE / CASH CONVERSION CYCLE (CCC)



WORKING CAPITAL CYCLE / CASH CONVERSION CYCLE (CCC)

Each component of working capital (namely inventory, receivables and payables) has two dimensions ....TIME .... and MONEY. When it comes to managing working capital - **TIME IS MONEY**.

If you can get money to move faster around the cycle like :

- ❖Collect monies due from debtors more quickly
- ❖Reduce the amount of money tied up by reducing inventory levels
- ❖Increase in credit period from suppliers

The business will generate more cash or need to borrow less money to fund working capital. As a consequence, you could reduce the cost of interest or additional *free* money available to support additional sales growth or investment. So, you effectively create *free* finance to help fund future sales.

Measuring a Company's Liquidity Through Cash Conversion Cycle

The Cash Conversion Cycle is a measure of working capital efficiency, often giving valuable clues about the underlying health of a business. The cash conversion cycle is comprised of three standard, so-called activity ratios relating to:

- **Turnover of inventory** (Raw Material – WIP –Finished Goods) (Assets)
- **Turnover of Trade Receivables** (Assets)
- **Turnover of Trade Payables** (liabilities)

The CCC tells us the time (number of days) it takes to convert these two important assets into cash.

MEASURING A COMPANY'S LIQUIDITY THROUGH CASH CONVERSION CYCLE

A fast turnover rate of these assets is what creates real liquidity and is a positive indication of the quality and the efficient management of inventory and receivables.

Raw Materials - W.I.P - Finished Goods - Debtors

Trade Payables **Cash Conversion Cycle**

Bank Borrowing +Long Term Fund

RATIOS OF CASH CONVERSION CYCLE

❖**Raw Material Holding Period**

= Avg. Stock of Raw Material *12/ Total yearly consumption of Raw material

❖ **WIP Holding Period**

= Avg. Stock of WIP *12/ Total cost of production for the year

❖ **Finished Goods Holding Period**

= Avg. Stock of Finished Goods*12/ Total cost of sales for the year

❖ **Receivable Turnover Period**

= Average Debtors *12 / total sales for the year

❖ **Account Payable Turnover period**

= Average Account Payable *12 / total purchase for the years

(for the calculation in days, multiply by 365 in place of 12)

SOURCE WORKING CAPITAL FINANCING

Working Capital is financed by following sources:

❖ **OWNED FUNDS**

A portion of long term funds, equity share capital and reserves & surplus is utilized to fund working capital

❖ **BANK BORROWINGS**

Various bank products like cash credit, Overdraft, Working Capital Demand Loan, Packing Credit, Bills Discounting, Factoring etc.

❖ **CREDITORS**

WORKING CAPITAL PRODUCTS

- Fund Based
  - Domestics
    - Cash Credit
    - Overdraft
    - Bills Discounting
    - WCDL
  - Exports
    - Pre-Shipment
    - Post-Shipment
- Non Fund Based
  - Letter of Credit
  - Bank Guarantee
- Structured Products
  - Factoring
  - Forfeiting
  - Corporate Loan
  - Commercial Paper
  - Securitization of Receivables
  - Buyer's/ Supplier's Credit

NON FUND PRODUCTS

❖Can be used to reduce cost of borrowed funds

❖Banks charge a small commission on Non fund based products as compared to interest on Fund based products

❖Usage of these tools is subject to a mutual understanding between the buyer and the supplier

NON FUND PRODUCTS - BANK GUARANTEE

Bank guarantee is issued by the bank undertaking the liability of applicant in case of his default. Guarantees may broadly be divided in three categories as under:

- **Financial Guarantees** - Guarantee to discharge financial obligation of the applicant

- **Performance Guarantees** – Guarantee for due performance of a contract by the applicant

- **Deferred Payment Guarantees** - Guarantee for the deferred payment in respect of capital item purchase

NON FUND PRODUCTS - LETTER OF CREDIT (L/C)

A document issued by a financial institution which provides an irrevocable payment undertaking to a beneficiary against complying documents as stated in the credit.

L/C facility can be assessed in the following manner:

	(Rs. In Cr.)
Total purchases	1000
Purchase under L/C (say 60%)	600
Period under L/C (days)	90
Lead time under L/C (days)	30
L/C Requirement (600 x (90 + 30)/365)	200

STRUCTURED PRODUCTS - FACTORING

❖Sale of receivables to outside agency specialized in the management of receivables.

❖Factoring can be with or without recourse basis.

❖**Advantages:**

(1) A ready source of short term funds

(2) Simple procedures/ documentation

(3) Require lesser margins

(4) Off balance sheet financing (without recourse)

STRUCTURED PRODUCTS - FORFEITING

❖Risk free option for exporters

❖Forfeiting agency purchases receivables at a discount from an exporter on a without recourse basis.

❖**Advantages:**

(1) Improved liquidity

(2) Convert credit sales into sales

(3) Credit limit does not get blocked

(4) Free from political risks

STRUCTURED PRODUCTS - CORPORATE LOANS

❖Secured/unsecured loan raised from financial institutions to meet the working capital requirement of a company.

❖Improves Net Working Capital.

❖Tenor 3 to 5 years

STRUCTURED PRODUCTS - COMMERCIAL PAPER

Commercial paper is one of the oldest instruments for raising short – term finance.

❖Some of the important guidelines issued by the RBI are as under:-

(1) Minimum TNW of Rs. 4 Crores.

(2) Has been sanctioned working capital limits by Banks/ all -India Financial Institutions

(3) Borrowal account must be standard asset.

(4) Minimum credit rating of P2 by CRISIL or equivalent.

(5) Maturity between 7 days to 1 year

(6) Issued in multiples of Rs. 5 lacs

❖Cheaper source of finance as compared to traditional bank finance

STRUCTURED PRODUCTS - SECURITIZATION OF RECEIVABLES

- Discounting of **<u>FUTURE CASH FLOW</u>**
- Cash Flows are not contingent on the performance of the borrowers.
- Cash flows are directly collected by the lenders or approved agencies.
- **<u>Examples:</u>**

(1) Rent Discounting

(2) Credit Card Discounting

(3) Royalty fees / Franchisee Fees Discounting

- **<u>Advantages:</u>**

(1) Better credit quality and hence easy in raising finance

(2) Lower cost of credit

(3) Without recourse financing in certain cases

(4) Balance sheet management

STRUCTURED PRODUCTS - SUPPLIERS'CREDIT and BUYERS'CREDIT

❖Suppliers' Credit: Short term loans where the credit for imports into India is extended by the overseas suppliers through a bank.

❖Buyers' Credit: Short term loans for payment of imports into India is arranged by the importer from a bank or FI outside India.

❖The funding banks primarily depend on the credit worthiness of L/C opening bank

ASSESSMENT OF WORKING CAPITAL

METHODS OF ASSESSMENT OF WORKING CAPITAL

1)TURNOVER METHOD

2)CASH BUDGET SYSTEM

3)COMMITTEE RECOMMENDATIONS

TURNOVER METHOD

Working Capital Requirement = 25% of Turnover

Promoter Contribution (Margin) = 5% of Turnover

Bank Finance = 20% of Turnover

- Proposed by The Nayak Committee

- Used for assessment of working capital needs of **SMALL TRADING COMPANIES**

- Not appropriate for big manufacturing and trading companies

Normally used for the financing of less than Rs. 25.0 lacs

CASH BUDGET

Cash Inflow –Cash Outflow = Bank Finance in the form of Working Capital

Cash Inflow as:
- Operating Income
- Capital Infusion

Working Capital Finance

Cash Outflow as:
- Salary
- Adm. & Selling Exp.
- Other operating expenditures

- Mainly used for **service sector companies Like BPO, KPO, Software companies etc.**
- Eliminates traditional requirement of Stock and Debtors for assessment

COMMITTEE RECOMMENDATIONS

Tandon Committee has recommended the following methods:

- **Method I -** Borrowers to bring 25 % of the net working capital (Current Assets –Current Liabilities)

- **Method II -** Borrowers to bring 25% of the Current Assets

- **Method III -** Borrowers to bring 100% of hard core assets + 25% of other current assets.

CORE CURRENT ASSETS, which has been defined by the Study Group as representing the absolute minimum level of raw materials, process stock, finished goods and stores which are in the pipeline to ensure continuity of production

COMMITTEE RECOMMENDATIONS

- ❖Under Method I the promoter has to bring minimum margin whereas the margin to be brought in under Method III is maximum
- ❖Chore Committee has discarded Method III and recommended Method II
- ❖Method II is also known as Maximum Permissible Bank Finance (MPBF)
- ❖Banks mainly use this method for assessment of Working Capital Requirements

In October 1993, the RBI infused operational autonomy by permitting banks to determine appropriate levels of inventory and receivables, based on production, processing cycle, etc. These lending norms were made applicable to all borrowers enjoying an aggregate (FUND-BASED) working capital limit of Rs.1 crore and above from the banking system.

COMMITTEE RECOMMENDATIONS

Example :

Raw Material	-	Rs. 56.0 cr.
Finished Goods	-	Rs. 45.0 cr.
Receivables	-	Rs. 80.0 cr.
Adv. to Suppliers	-	Rs. 15.0 cr.
Credit Payable	-	Rs. 30.0 cr.

(Minimum requirement of Raw Material and Finished Goods is Rs. 15.0 cr. and 10.0 cr. respectively)

COMMITTEE RECOMMENDATIONS

Computation of MPBF:

Method I :

A - Total Current Assets	196.0
B - Less: Current liab.	30.0
C - Net Current Assets (A-B)	166.0
D – Less 25% margin on NCA	41.5
E – MPBF (C-D)	124.5

Method II :

A - Total Current Assets	196.0
B - Less: Current liab.	30.0
C - Net Current Assets (A-B)	166.0
D – Less 25% margin on TCA	49.0
E – MPBF (C-D)	117.0

COMMITTEE RECOMMENDATIONS

Method III :

A - Total Current Assets	**196.0**
B – Core Current Assets	25.0
C - Less: Current liab.	30.0
D - Net Current Assets (A-C)	166.0
E – Less 25% margin on TCA other than CCA (196.0-25.0)	42.75
F – Less 100% margin on CCA (25.0)	25.0
G – MPBF (D-E-F)	**98.25**

CREDIT MONITORING ARRANGEMENT

RBI has mandated a certain way of analyzing the financial statement i.e. CMA.

The break-up of assets and liabilities in CMA differ slightly from that mandated by the company law board (CLB)

- Form I Particulars of Existing & Proposed Limits
- Form II Operating Statement
- Form III Analysis of Balance Sheet
- Form IV Comparative Statement of Current Assets & Current Liabilities
- Form V Computation of Maximum Permissible Bank Finance (MPBF)
- Form VI Funds Flow Statement

CREDIT MONITORING ARRANGEMENT

Example of difference in

Particulars	As per Schedule VI	As per CMA
Liabilities		
Int. on TL accrued	Long term Liabilities	Current Liabilities
Install. Of TL due within 1 year	Long term Liabilities	Current Liabilities
Debentures/bonds/Pref. Shares due in next 1 year	Long term Liabilities	Current Liabilities
Assets		
FDRs as margin for non fund based limit	Current Assets	Non –Current Assets
Debtors with more than 180 days	Current Assets	Non –Current Assets
Old stock	Current Assets	Non –Current Assets
Short term Advance or loan to other corporate	Current Assets	Non –Current Assets

FINANCIAL RATIOS

In general, there are 4 kinds of financial ratios that a financial analyst will use most frequently, these are:

- ❖ **Performance ratios**
- ❖ **Working capital ratios**
- ❖ **Liquidity ratios**
- ❖ **Solvency ratios**

These 4 financial ratios allow a good financial analyst to quickly and efficiently address the following questions or concerns:

FINANCIAL RATIOS - PERFORMANCE RATIOS

❖**What return is the company making on its capital investment?**

❖**What are its profit margins?**

- Operating Profit to Net Sales = Operational Profit / Net Sales
- Gross Profit to Net Sales = Gross Profit / Net Sales
- Net Profit to Net Sales = Net Profit / Net Sales
- Net Profit to Networth = PAT /Networth (Shareholder Fund)
- Return of Capital Employed = PAT / Net Worth + Net WC
- Net Sales to Total Assets = Net Sales / Total Assets

FINANCIAL RATIOS - WORKING CAPITAL RATIOS

- **How quickly are debts paid?**
- **How many times is working capital cycle turned?**

•Debt Service Coverage Ratio (DSCR) =

PAT + Depreciation +Interest on TL/ Install. of TL +Int. on TL

•Interest Service Coverage Ratio (ISCR) =

PAT + Depreciation + Interest / Interest

•Stock Turnover Ratio = Cost of sales / Average Inventory

•Debtors Turnover Ratio = Credit Sales or Sales/ Average Debtors

•Creditor Turnover Ratio = Credit purchase or purchase / Avg creditors

FINANCIAL RATIOS - LIQUIDITY RATIOS

❖**How quickly are Current Assets can be realized and Current Liabilities can be paid off?**

- **Can the company continue to pay off its liabilities and debts?**

- <u>Current Ratio</u> = Current Assets / Current Liabilities
- <u>Quick Ratio</u> = Quick Assets / Quick Liabilities

FINANCIAL RATIOS - SOLVENCY RATIOS (LONGER TERM)

❖**What is the level of debt in relation to other assets and to equity?**

❖**Is the level of interest payable out of profits?**

• <u>Debt Equity ratio</u> = Debt/ Equity

• <u>Equity to Net Fixed Assets Ratio</u>

= Shareholder Fund (Capital + reserve) / Net Fixed Assets (Net Block)

SPECIAL SITUATIONS FOR ASSESSMENT OF WORKING CAPITAL

- ❖CYCLICAL PRODUCTION/SALES
- ❖ PHASED EXPANSION PROGRAMS
- ❖ MAJOR ORDERS
- ❖ ENHANCEMENT DURING THE YEAR
- ❖ CORPORATE LOAN
- ❖ DRAWING POWER NOT ALLIGNED TO MPBF
- ❖ DEVALUATION / EROSION OF CURRENT ASSETS

CYCLICAL PRODUCTION/SALES

❖**CASE**

•The company's business is cyclical in nature

•May –Aug: Peak Level Activity

•Seasonal Production and Seasonal Sales

❖ **ACTION**

•Use of average production or sales to assess Working Capital will not give proper assessment of Working Capital requirement in Peak level as well as normal activity.

•Both normal and peak level working capital requirements should be assessed separately.

❖ **Advantages:** Better operations management and prevent liquidity crunch during peak level.

PHASED EXPANSION PROGRAMS

❖**CASE**

•The company is undergoing a Phased Expansion

•Expansion is on a machine-by-machine basis

•Current Assets and Current Liabilities will build up gradually

❖ **ACTION**

•Assessment of Working Capital on the basis of average sales will not reflect actual Working Capital requirement.

•Assessment should be done based on the peak level activity.

•Drawing Power will be released on the built up of Current assets and Current Liabilities

•As initially low working capital is required and later higher working capital is required

❖**Advantages:** No under-finance and no multiple assessment

MAJOR ORDERS

❖**CASE**

- The company’s major sales and purchases take place in bulk orders
- Bulk orders are not very frequent
- Basic Working Capital requirements prevail throughout the year

❖**ACTION**

- Assessment of Working Capital requirement on the basis of average level of activity will not reflect actual Working Capital Requirement.
- Assessment should be done on order-to-order basis.

❖**Advantage:** Prevents liquidity crunch while handling major orders.

CORPORATE LOAN

Corporate loan is an effective Working Capital Management tool, when:

- Short term funds used in acquisition of long term assets
- Low current ratio, with very low debt equity gearing
- Acquisition of business

EXAMPLE - Current Financial Position of the Company

Net Worth	Rs. 100 cr	Net Block	Rs. 100 cr
Term Loan	Rs. 20 cr	Current Assets	Rs. 145 cr
WC Limits	Rs. 110 cr	Creditors	Rs. 15 cr
Current ratio:	1.16	Debt to Equity:	0.20

Company may avail a Corporate Loan of Rs. 20 crores or more to shore up the Current Ratio to 1.33 subject to adequate FACR / ACR.

MAXIMUM PERMISSIBLE BANK FINANCE (MPBF) LIMITATION

- Represents position on a particular date
- Not tuned to Peak Time Assessment
- Not applicable for service industries
- In practice, may differ with Drawing Power

DRAWING POWER NOT ALLIGNED TO MPBF

Many times Drawing Power is not aligned with MPBF due to various reasons:

❖Margin stipulations

❖Amount of current assets other than Stock and Debtors

❖Sub Limits Stipulation

❖Number of days stipulation

DRAWING POWER NOT ALLIGNED TO MPBF

EXAMPLE

Current Assets and Liabilities of the Company are:

Creditors : RS. 50 crores

Stock: Rs. 140 crores

Book Debts: Rs. 200 crores (Rs. 20 crores more than 90 days)

Other Current Assets: Rs. 10 crores

Total Current Assets: Rs. 350 crores

Sanctioned Bank Limit : Rs. 210 Crores (sub limits on Debtors Rs. 100 crores)

<u>**Stipulations:**</u>

Margins:

Stock 25%

Debtors 35% (up to 90 days)

DRAWING POWER NOT ALLIGNED TO MPBF

MPBF

A - Total Current Assets	350.0
B - Less: Current liab.	50.0
C - Net Current Assets (A-B)	300.0
D – Less 25% margin on TCA	87.5
E – MPBF (C-D)	212.5

Drawing Power

A – Paid Stock (140-50)*75%	67.5
B – Debtors (200-20)*65%	117.0
C – Drawing Power (A+B)	184.5

- Present Drawing Power Rs.184.5 Crores is much less than sanctioned Limit Rs. 210 Crores
- The Company should approach the Bank to reduce margin on Debtors to 25%

DRAWING POWER NOT ALLIGNED TO MPBF

<u>Example -2</u>

Creditors	: RS. 50 crores
Stock	: Rs. 140 crores
Book Debts	: Rs. 170 crores (Rs. 20 crores more than 90 days)
Advances to suppliers	: Rs. 90 crores
Other Current Assets	: Rs. 10 crores
Total Current Assets	**: Rs. 400 crores**
Sanctioned Bank Limit	: Rs. 210 Crores

<u>Stipulations: </u>Margins:

Stock 25%

Debtors 35% (up to 90 days)

DRAWING POWER NOT ALLIGNED TO MPBF

MPBF

A - Total Current Assets	**400.0**
B - Less: Current Liab.	50.0
C - Net Current Assets (A-B)	350.0
D – Less 25% margin on TCA	100.0
E – MPBF (C-D)	250.0

Drawing Power

A – Paid Stock (140-50)*75%	**67.5**
B – Debtors (170-20)*65%	97.5
C – Drawing Power (A+B)	165.0

- Present Drawing Power Rs.165.0 Crores is much less than sanctioned Limit Rs. 210 Crores
- Approach the Bank to - Reduce margin on Debtors to 25%
- Take the Overdraft facility against Advance to supplier to Fund WC.

DRAWING POWER NOT ALLIGNED TO MPBF

Example -3

For the transport company having 300 vehicles financed from bank for the tenor of 4 years

Creditors	: RS. 50 crores
Other current liabilities	: Rs. 15 crores
Stock	: Rs. 100 crores
Book Debts	: Rs. 210 crores (Rs. 20 crores more than 90 days)
Other Current Assets	: Rs. 40 crores
Total Current Assets	: **Rs. 350 crores**
Sanctioned Bank Limit	: Rs. 180 Crores

(Total Term Loan outstanding is Rs. 322.0 crores, payable within 1 years is Rs. 65.0 cr.)

Stipulations: Margins:

Stock 25%

Debtors 35% (up to 90 days)

DRAWING POWER NOT ALLIGNED TO MPBF

Profit & Loss Data

Turnover	-	Rs. 828.0 cr.
Total operating Cost	-	Rs. 678.96 cr.
Interest On WC	-	Rs. 21.0 cr.
Interest on Term Loan	-	Rs. 26.1 cr.
Depreciation	-	Rs. 54.74 cr.
PBT	**-**	**Rs. 47.2 cr.**

DRAWING POWER NOT ALLIGNED TO MPBF

MPBF

A - Total Current Assets	350.0
B - Less: Current liab.	130.0
C - Net Current Assets (A-B)	220.0
D – Less 25% margin on TCA	87.5
E – MPBF (C-D)	132.5

Drawing Power

A – Paid Stock (100-50)*75%	37.5
B – Debtors (210-20)*65%	123.5
C – Drawing Power (A+B)	161.0

- Present Drawing Power Rs.161.0 Crores is much less than sanctioned Limit Rs. 180 Crores
- Approach the Bank to Reduce margin on Debtors to 25%
- Not to include the TL inst. Payable in 1 year in CL to calculate the MPBF

DRAWING POWER NOT ALLIGNED TO MPBF

Revised MPBF

A - Total Current Assets	**350.0**
B - Less: Current liab.	65.0
C - Net Current Assets (A-B)	285.0
D – Less 25% margin on TCA	87.5
E – MPBF (C-D)	197.5

SECURITIES

❖**Primary**

- **<u>Working Capital Loan –</u>** Charge on the Current Assets
- **<u>Term Loan -</u>** Charge on the fixed Assets, mainly the assets financed by the loan

❖**Collateral**

- Mortgage over the immovable property
- Hypothecation on the movable machineries like vehicles etc.

❖ **Guarantee**

- Personal
- Corporate

WORKING CAPITAL vs. TERM LOAN

Term	WORKING LOAN	TERM LOAN
Nature	Short Term	Long Term
Period	1 year and thereafter renewed annually	More than 1year and reviewed annually
Purpose	Meeting the working capital gap of the firm	Mainly for capital expenditure like purchase of Fixed Assets, establishment of business etc.
Rollover	It is rollover facility	It is a non rollover facility
Primary Security	Charge over the current assets	Charge over the fixed assets and mainly the assets financed by the loan

LOAN DOCUENTS PROCEDURE

Post Sanction Documents are an integral part of the financing.

The documents will be dependent upon the condition as well as security to be created.

❖Accepted Copy of Sanction letter.

❖Copy of Board Resolution for the acceptance of the sanction with authorization to sign the bank documents and creation of the security as per the sanction letter.

❖Copy of MOA/AOA of the company

❖Main Facility Agreement / Master Facility Agreement

❖Demand Promissory note on the letter head of the Company (with Revenue Stamp)

❖Deed of Hypothecation on Stamp Paper As applicable

❖Deed of Guarantee on stamp Paper as applicable (Personal / Corporate)

❖Various undertaking on the stamp paper as per the terms of the sanction letter

❖Certificate u/s 281 (1) of the Income Tax Act 1961.

❖Signing of Form 8 and 13 under the Companies Act, 1956, with regard to creation of the charge in ROC.

❖In case of Multiple or Consortium Arrangement, exchange of the pari - passu charge / second charge on the security, as per the term of the sanction letter

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

❖Business Plan / Project report is a critical activity for every project whether for the new venture or the enhancement in the current operation of the business.

❖It is the basic data which is very important for taking the decision for capital investor, State Holder, Creditors and Bank, NBFC and FIIs.

❖The Broad Line of the DPR will depend on the activity of the business and ultimate objective of the DPR. The DPR should includes the following information:

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

<u>Index of the Contents of DPR</u>

1. Executive Summary
- ❖Mission
- ❖Vision
- ❖Objective
- ❖Overview of the entire project

2. Brief of the project

3. Brief about the demand / justification of the project
- ❖Past Trend
- ❖Industry Data
- ❖Change in the technology / policy to raise the demand for new project
- ❖Project rational
- ❖Specific advantage of the project to company

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

4. Market and Sales

- ❖Basic market orientation: local, national, regional, or export.
- ❖Projected production volumes, unit prices, sales objectives, and market share of proposed venture.
- ❖Potential users of products and distribution channels to be used. Present sources of supply for products.
- ❖Future competition and possibility that market may be satisfied by substitute products.
- ❖Tariff protection or import restrictions affecting products.
- ❖Critical factors that determine market potential.

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

5. Technical feasibility, manpower, raw material resources, and environment:

- ❖Brief description of manufacturing process.
- ❖Comments on special technical complexities and need for know-how and special skills.
- ❖Possible suppliers of equipment. Ideally three competitive quotations to be enclosed.
- ❖Availability of manpower and of infrastructure facilities (transport and communications, power, water, etc.).
- ❖Breakdown of projected operating costs by major categories of expenditures.
- ❖Source, cost, and quality of raw material supply and relations with support industries.
- ❖Import restrictions on required raw materials.
- ❖Proposed plant location in relation to suppliers, markets, infrastructure and manpower.
- ❖Proposed plant size in comparison with other known plants.
- ❖Potential environmental issues and how these issues are addressed.

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

6. Promoters, Management and Technical Assistance

- ❖Shareholding pattern
- ❖Promoter's profile including financial information
- ❖Directors and other key personal profiles
- ❖Description of technical arrangement (Production, Marketing, Finance etc.)

7. Project Plan

8. Implication Schedule

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

9. Project Cost

- ❖Estimate of total project cost, broken down into
  - •Land,
  - •Construction of buildings and civil works,
  - •Plant and machinery,
  - •Miscellaneous fixed assets,
  - •Preliminary and preoperative expenses and
  - •Working capital.

10. Means of Finance

- ❖Equity
- ❖Debt
- ❖Loan

PREPARATION OF BUSINESS PLAN / PROJECT REPORT (DPR)

11. Financial Assumptions

12. Financial projections

- ❖ Profit & Loss account
- ❖ Balance Sheet
- ❖ Cash Flow
- ❖ Fund Flow
- ❖ Project IRR / Equity IRR
- ❖ Pay Back Period
- ❖ Debt Service Coverage Ratio/Int. service Coverage Ratio

13. SWOT Analysis

- ❖ Strength
- ❖ Weakness
- ❖ Opportunities
- ❖ Threats

THANK YOU